FREE TRADE AND THE YUKON

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by the

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Canada US Free Trade - How Should the Yukon React?

The purpose of this brief is to make available to the Yukon Economic Council the views of the Canadian Labour Congress and its affiliated unions on the issue of Canada US free trade.

The CLC and its affiliated unions have taken an active part in the debate on free trade, and we have stated our views aggressively, because we believe that the interests of our members, as workers and more generally as Canadians, are affected by the outcome of the free trade talks.

In our view, it is important that the debate on free trade, and the much wider debate on economic options for Canada, not be confined to the "experts". Economic policy is about making choices, and it is about how we want to live, as Canadians. The proper choices cannot be seen simply as technical ones; they require input from the people affected.

Free Trade, or Freer Trade?

The first point that should be established is that we are, in fact, talking about free trade, not simply freer trade, or "enhanced trade" or any other of the many euphemisms that have been used to describe the current negotiations and their likely outcome.

There have, in the past, been exercises to "enhance access" to certain parts of the US market for some types of goods, and these attempts have met with varying degrees of success.

These attempts include both bilateral deals, between the United States and Canada alone, and multilateral deals, through the GATT, the General Agreement on Trade and Tariffs.

There have been two rounds of GATT negotiations which have had a profound effect not just on our trade with the rest of the world in general, but with the United States in particular. In addition, there have been bilateral deals such as the Auto Pact and the Defence Production Sharing Agreement. All of these have had an affect on Canada Us trade. In addition, there were a series of attempts in the late 1970's and early 1980's to negotiate sectoral agreements between the United States and Canada, attempts which were ultimately unsuccessful, but which suggest other strategies for trade policy than the one before us.

Multilateral Trade Initiatives

The last two rounds of GATT negotiations, the Kennedy Round, which finished in 1967, and the Tokyo round, which finished in 1979, substantially reduced tariff and non tariff barriers on a wide range of goods between member countries, including Canada and the US.

The Kennedy Round, which finished in 1967, produced tariff cuts averaging about 35% across the board; duties were reduced on about 70% of the value of dutiable imports in the GATT area, and tariffs were cut 50% or more in almost two thirds of the cases.

The Tokyo Round further reduced trade barriers. In fact, by the end of 1987, when the staged reductions in tariffs that resulted from the Tokyo Round are fully in place, about four fifths of Canada's exports to the United States will be free of tariffs, and about two thirds of Canada's imports from the United States will be free of tariffs. A large proportion of the remaining trade between the two countries will take place at tariffs of 5% or lower. In other words, the bulk of items being traded between the two countries after 1987 will be either free of tariffs or trading at tariffs low enough so that other factors such as the exchange rate, marketing, security of supply, quality of goods and so on are likely to be more important than tariffs.

These cuts represent a substantial change in the conditions under which goods trade within the GATT area, including within the Canada US area. As a result of these two rounds of tariff cuts, for instance, large proportions of our resource trade already moves into the United States market free of tariffs. The best known example of this is in the lumber area, where softwood lumber currently moves into the US market tariff free.

In fact, the GATT talks have been so successful in lowering tariff barriers between member countries that tariffs are not, in fact, the major issue at stake in current trade talks, either in the upcoming GATT talks which will begin sometime in late 1986, nor in the Canada US talks, which, by and large turn on two related issues, non tariff barriers and security of access. (both of which are discussed in more detail below)

In summary, then, GATT negotiations in the past have been a major factor in reducing trade barriers between member countries, and that includes, of course, between Canada and the US.

Upcoming GATT negotiations may well provide, again, the opportunity to address a number of these trade related problems, including the problem of access to the US market.

Bilateral Trade Initiatives

A. The Auto Pact

In addition to the multilateral trade initiatives, there have in the past been a number of sector specific trade initiatives between Canada and the United States. The most well known are the Auto Pact and the Defence Production Sharing Arrangement.

The Canada US Automotive Products Trade Agreement (Auto Pact) was signed in 1965 and resulted in a substantial increase in the auto related trade between the two countries. Moreover, as a result of the safeguards built into the agreement, Canada experienced a substantial increase in jobs in the auto industry, and in spinoff activities.

This kind of sectoral trade agreement represents an alternative to the kind of overall trade deal that seems to be contemplated with the current free trade talks. However, about the Auto Pact a couple of points need to be made.

FIrst, the Auto Pact is not an example of free trade, but of managed trade. The Auto Pact allows for the duty free movement of cars and some parts across the border, but only on condition that production in Canada is above a certain level, which is related to sales in Canada. In other words, the large auto makers who benefit from the Auto Pact, have to guarantee a certain minimum amount of investment, and therefore jobs, in Canada as a condition of the duty free entry of their cars.

This minimum level of investment has been a major source of controversy at various times in the past, as some of the auto makers fell temporarily below the required investment levels. The less of the Auto Pact would seem to suggest that policing investment and jobs safeguards of this kind requires active government monitoring of the industry, and the willingness to get tough with the industry when necessary. A government ideologically committed to non intervention in market decisions such as investment is not likely to be able to extract the maximum advantage from such an arrangement.

Second, the kinds of safeguards that were won in the Auto Pact are not likely to be repeated in the 1980's. In order to be acceptable, they require a GATT waiver, which was granted only after much debate in the early 1960's and is not likely to be repeated now, in the kinds of industrial sectors that might be subject to such a pact. Moreover, they require US agreement, which is just as unlikely in the context of large job losses in most US industrial sectors in recent years.

Finally, it should be noted that the Auto Pact resulted in labour and other adjustments that took roughly a decade to sort out. This is in the context of a growing industry where jobs were increasing, not decreasing. Such sectoral arrangements require transitional adjustment schemes that are generous enough to handle the employment displacement that inevitably happens with structural change, and long lasting enough to catch all of the adjustment problems as they happen, some of them some years after the original agreement.

These comments are particularly relevant since Prime Minister Mulroney has commented recently that, in fact, the free trade talks may not result in overall free trade at all, but in a series of industry specific pacts similar to the Auto Pact in intent. If this is the case, the lessons of the Auto Pact are particularly relevant.

B. The Defence Production Sharing Agreement

The Canada US Defence Production Sharing Agreement was signed in 1959, and allowed for national treatment of both countries' defence industries by the other country. In other words, with some exceptions, related to national security provisions, defence contractors and manufacturers of defence related equipment were to be allowed to bid on contracts in either country as if they were a company resident in that country.

The DPSA has, in fact, resulted in sales of Canadian military equipment to the United States, although we also buy substantial amounts of US equipment.

However, if the Auto Pact illustrates one particular problem with bilateral deals with the US, the DPSA illustrates quite another set of problems.

As is discussed in more detail below, the US Constitution is such that domestic federal law takes precedence over international agreements. This has resulted in a number of problems with getting the full access that had been expected of the DPSA, which, at least in theory, represents free trade in military equipment and supplies but which in practice has fallen far short of it.

To begin with, the DPSA has been breached over the years because of the Buy America Act, a 1933 federal law which has wide implications for US federal procurement. In the future, even after a free trade pact, we could expect similar problems, either with the Buy America Act itself, or with other similar acts. (The Buy America Act is discussed in more detail below.)

Secondly, national security has proven to be a much more important factor in trade restrictions than had been thought in 1959. It can be expected that this would continue even after a free trade pact.

As well, US laws designed to keep defence related jobs at home rather than in other countries have proven difficult to counter, and could be expected to continue. The best example of this is the recent loss of 350 jobs at St. John Shipbuilding and Drydock because of the loss of a subcontract on an American Navy cruiser. The loss was due to the Burns Tollefson Clause, a standard clause which is inserted in US government procurement bills on major military equipment and requires all major subcontract work to be

done by US companies, in the US. This particular incident illustrates the problem of getting secure access to the US market in the fact of determined efforts to block that access, even when international agreements provide for free trade.

The Lessons of the Past - Multilateral or Bilateral Deals?

The lessons of the past would suggest that multilateral trade talks are a safer, and more effective way to reduce trade barriers, not only between Canada and the rest of the GATT countries,but between Canada and the US.

As the above discussion suggests, the GATT talks have been successful in achieving dramatic reductions in trade barriers in the past, while bilateral deals with the United States, while sometimes effective, are not always as effective as Canadians had hoped they would be.

The next round of GATT talks will center on the reduction of non tariff barriers, just that area that will be of most controversy in the Canada Us trade talks. If that is the case, why risk negotiating bilaterally with a trade partner which is in its most protectionist mood in many years and is determined to reduce its trade deficit with the rest of the world, including Canada, for trade guarantees which may not be delivered if they threaten US jobs?

Attached are two lists of trade related measures, which illustrate the difference between the risks involved in bilateral and multilateral approaches to trade.

The first consists of a series of trade related measures that are allowed under the GATT. As the list notes, they range from import and export controls to emergency powers to limit imports if there is concern about their danger or about their effect on jobs, to the ability to apply countervailing duties to a wide range of products if it is felt they endanger domestic industry.

These are all measures which are consistent with our obligations to GATT, and which Canada and many other GATT countries have used and continue to use to protect their domestic industry. These powers are not up for discussion under the Canada US free trade talks. The ability to invoke the emergency GATT provisions on items like cedar shakes and shingles, for instance, is not on the table for negotiation. Nor is the ability to apply countervailing duties on softwood lumber, such as may possibly be the case in a few months. These are powers that both Canada and the US as GATT signatories, will retain, whatever the outcome of the bilateral trade talks.

The second list is a list of non tariff barriers to trade, not all of which were originally enacted to meet trade related purposes, but most of which the US negotiators have identified as non tariff barriers which are up for discussion in the free trade talks.

The significance of the second list is that it is at the same time a list of those powers which Canada has retained even after several rounds of GATT talks, and a list of those powers which are likely to come under fire in a free trade deal with the United States.

A quick perusal of the list will suggest that it contains a number of tools of economic management which are basic to government economic planning, a number of programmes which have preserved a large number of jobs in Canada, and a number of policies which were enacted to preserve cultural industries.

These non tariff barriers have been consistent with our membership in GATT, but might be at risk in a bilateral trade deal with the US.

In short, a free trade deal with the US would leave intact all of the measures which have been used, for instance, against the forest industries in recent months, while putting at risk a number of what the Americans regard as non tariff barriers but which we have seen as basic policies and programmes.

Free trade with the US, then, should not be seen as simply an extension of the trade liberalization with which we have been associated as a country since the end of the Second World War. It is not simply an acceleration or an extension of the current practice of moving toward multilateral trade liberalization. It is a change in practice, and a move toward a quite different form of trading relationship, with both the United States and the rest of the world.

This is especially so when the free trade initiative is put n the context of a wider policy direction in the United States toward protectionism. To the extent that Canada becomes more closely tied in to the American economy through a free trade arrangement, it becomes part of what some have described as a "fortress America" approach to trade issues.

Paradoxically, then, to be in favour of free trade in this context is to be in favour of protectionism toward the rest of the world.

We can assume, for instance, that under a free trade arrangement with the United States, when goods are travelling freely across the border, Canadian policy makers will be under pressure to impose the same kinds of barriers to the entry of foreign goods that the Americans are imposing. Otherwise, Canada could become a conduit for the entry into the United States of just those kinds of goods which the Americans are most concerned to exclude.

Free trade, then, is likely to have a profound, and perhaps negative, effect on our trading relationships with the rest of the world.

To the extent that regional economies in Canada depend on the export of goods to areas of the world other than the US, this could be a significant factor in deciding how to react to the trade talks. The Yukon, for instance, might want to consider the impact of free trade and closer Canada US economic relationships on this trade.

In short, contrary to arguments voice by some, free trade with the US is not necessarily consistent and parallel with general trade liberalization under GATT. It is an alternative. If we are interested in preserving our status as a trading nation, and in gaining access to a large market for our goods, we are faced with either doing it through multilateral GATT talks, which will also liberalize our trade with the US, or doing it through bilateral free trade talks, which are likely to undermine our relationships with other GATT countries without necessarily giving us the unimpeded access that we seek to the US market.

Will We Get Secure Access To the US Market?

A central argument in the free trade debate has to do with the importance of secure access to the US market. In the face of our growing export dependence as a country on this one market, any protectionist moves to cut off imports would be disastrous to the Canadian economy.

We are a lot more dependent on the US market than they are on us. This point is made in the DPA brief, but it is used to buttress the argument that we need to secure access now, before protectionism in the US does damage to us, either deliberately or inadvertently.

How likely is it that we will get this secure access?

1. Countervailing Duties

Let us look first at the issue of countervailing duties, which has arise in the case of softwood lumber exports to the US. Several American representatives have already answered in the negative when asked if we are likely to get relief from these provisions of trade law.

The free trade pact between Israel and the US did not provide for relief from this provision.

The ability to apply countervail and anti dumping measures is part of the GATT agreement, it is not part of the Article XXIV provisions under which a comprehensive free trade arrangement would be signed, and since the removal of this provision for one country and not for all the other signatories to Gatt would amount to discriminatory practice, we can be sure that this is simply out of the question.

It may be argued that the recent use of the countervail provisions on cedar shingles and shakes, for instance, indicates even more the urgency with which we need to sign a free trade agreement with the US. In fact, as it is certain that we will not get exemption from this provision, this argument is rather misleading. A more compelling argument would suggest that the US willingness to use these provisions at the same time that highly sensitive free trade talks are going on between Canada and the United States, talks that could possibly be jeopardized by the use of countervail at this time, indicates the importance the Americans put on the right to use countervail provisions to protect their domestic industry.

2. Non Tariff Barriers

The second point has to do with non tariff barriers of all kinds that impede trade between the two countries. The list of Canadian non tariff barriers reproduced here suggests how long such a list can be, and it is clear that this particular list contains a number of items, for instance the culturally related items, that we are not likely to give up in an free trade negotiations. Similarly, it can be assumed that the Americans will have a long list of such items that they will resist giving up as well.

Consider the attached document from the Department of External Affairs referring to "Buy American" practices. These practices abound at both the federal and state levels.

At the federal level the Buy American provisions are embodied in the Buy America Act of 1933, which limits sales opportunities for foreign producers, including Canadian producers by establishing barriers against the purchase of foreign goods by US federal departments and agencies.

Many government departments go beyond the Buy America provisions in enforcing their own procurement policies, not all of which are formal or embodied in regulations.

Prime contractors with the US federal government are required to follow the Buy America Act in subcontracting work. In general this is done through a standard clause in US government procurement contracts that specifies domestic end products and use of domestic subcontractors.

In this respect, it should be pointed out that these clauses, and the laws on which they are based have, under the US constitution, precedence over international agreements.

Finally, consider the attached list of state Buy America provisions. Again, not all state buy local policies are necessarily in legal code from; some are implemented through attitude and buying preference.

The number of states with these provisions, as the document suggests, is increasing. Moreover, such provisions are controlled by the federal government only with great difficulty.

Alaska, it should be noted, does have such a price preference system that provides a significant advantage to in-state suppliers of goods to the state government. This price advantage, perhaps, is less significant that it would otherwise be because of the current exchange rates; on the other hand, a rise in the exchange rate of the Canadian dollar, a factor which it is not within the ability of local suppliers to control, could eliminate any price advantage held by Canadian suppliers very quickly.

3. Exchange Rates

The third factor that is likely to impede our access to the market is a rise in the exchange rate of our dollar as compared to that of the US.

Many of our products are competitive in the US market only because of the low exchange value of our dollar. This is a fact that is not lost on the Americans. In fact, the US Secretary of the Treasurer has suggested, recently, that the Canadian dollar is significantly undervalued and that Canada has an obligation to its trading partners to revalue upward.

Such a revaluation upward would, of course, be in line with American concerns, since we are currently running a large ($20 billion a year) trade surplus with them which has resulted in job loss in the United States. A revaluation upward, however, would undoubtedly mean job loss in Canada.

It is difficult to say just what proportion of the goods produced in the Yukon might be highly vulnerable to a change in our exchange rate, but it is clear that some parts of the economy would be affected, for instance the minerals sector, and that more research on this vital question needs to be done.

It is clear, however, that US pressure on Canada to revalue its dollar upwards will continue.

As the attached chart from the Wood Gundy report suggests, the purchasing power parity level of the Canadian dollar has fallen significantly in recent years compared to the US dollar.

Wood Gundy, in its latest forecast (The Canadian Economy Through 1988, May 16, 1986) suggests that the dollar will probably move upward from a current value of roughly $US .7170 (i.e. a Canadian dollar is worth 71.7 cents US) to a range of US .75 or .76 by 1988. Such a rise represents roughly a 6% increase in the exchange value of the Canadian dollar, and could wipe out the competitive advantage that many Canadian industries, including perhaps some in the Yukon, currently enjoy.

All of these considerations suggest that secure access to the US market may not be assured as has been assumed by free trade proponents.

Can Canada Expect Overall Gains From Free Trade

Before examining some factors mores specific to the Yukon, it is worthwhile to examine some of the issues that arise for Canada as a whole. There is already a large literature on the supposed economic gains to be had from free trade, and it is worth looking briefly at some of the questions that arise, since it is unlikely that Yukoners would gain from a deal that did not provide overall benefits to the Canadian economy.

The argument is made, in the consultant's report delivered to the Economic Council and elsewhere, that economic studies suggest a sizable overall gain in welfare from bilateral free trade.

> to the extend that economic gains are estimated in previous studies for the total country are realized in Yukon, free trade would add between $600 and $1300 to the average per capita incomes of Yukon residents

The study referred to (Cox and Harris, 1985) is worth examining, briefly, since it is referred to frequently and since the reference to the study,and the numbers suggested by it, lend an air of exactness to the question of predicting the outcome of free trade with the US.

Cox and Harris suggest that the effect of free trade with the US could be an increase in the output in the Canadian economy of up to 9% based on productivity gains of up to 30% in Canadian manufacturing, and an increase in employment of up to 5.5%.

The federal government, in documents released earlier this year, (Canadian Trade Negotiations, dated December 1985, released spring 1986) estimates a GNP gain of 3-8% from the effects of bilateral trade, based on similar reasoning.

As Bruce Wilkinson has suggested in a critique of the Cox Harris study (Wilkinson, 1985, attached) the results of the study are highly questionable, and "Canada should not be negotiating a free trade agreement with the US under the assumption that such estimates are realistic."

As Wilkinson has suggested, the Cox Harris study is based n data on tariffs and structural elements in the Canadian economy that are at least a decade old. The fail to account, for instance, for the Tokyo round of tariff reductions, and the structural adjustments in the economy as a result of these reductions. Their conclusions, then, about the affect of tariff reductions resulting from bilateral free trade are likely to be exaggerate.

The estimates of the productivity gains to be had from the removal of tariff and non tariff barriers, as well, are likely to be overstated. As Wilkinson notes, after seven rounds of GATT negotiations, Canadian productivity in manufacturing remains 25-30% below that in the US, yet the study assumes productivity equal to that of the US will result from free trade. It is more likely that some productivity gap will remain, even after a free trade post is signed.

With respect to the scale economies argument, it should be noted there are serious questions. Recent work done by the Economic Council of Canada (Daly and Rao, 1985) suggests that the economic gains to be had from economies of scale in the context of Canada Us free trade may be extremely limited.

The economies of scale effect will accrue, if it accrues, to mass production operations mostly in Ontario. There is no reason to think it will be evenly based in regional terms. Nor is there any reason to think it will be evenly based in terms of large and small operations.

With respect to the Yukon, whose manufacturing is small scale and which is not likely to gain from the kinds of economies of scale that are assumed in the Cox Harris study, it would be extremely dangerous to simply take the average gains referred to in the study, overstated or not, and apply them in an arithmetic fashion to the Yukon economy.

It should be noted however, that some producers in the Alaskan economy would undoubtedly be large enough to capture some economics of scale in specialty manufacturing, and perhaps other areas, and would be in a position to compete in the Yukon markets if there were any significant movement in exchange rates.

There is, moreover, no reason to think that any income gains from economies of scale and increased productivity will be generally dispersed between owners and workers. In fact given the highly concentrated nature of the Canadian economy, the lack of competition in many markets (e.g. the Yukon) the welfare gain may occur in the form of higher profit margins, not higher living standards or incomes. To some this may be a plus, to others it may be seen as a drawback.

All of these considerations, and some others, suggest that the employment gains suggested by this study are highly questionable.

There is reason to believe that the removal of the remaining tariff walls around Canada would result int he shift of at least some firms back to the United States; this would be so even if legislation and other social conditions in the two countries were equal, if for no other reason than that the US market is ten times as large as that of Canada. However, there is a well documented

shift in production and employment within the United States itself from the traditional industrialized parts of the country to those parts of the country where union security, minimum wages, industrial and social legislation which increases the cost of doing business, and the role of unions in general, are not significant factors. We can assume a similar phenomenon in Canada once there are no economic borders to prevent goods being shipped into Canada from these parts of the US.

These comments suggest that the macro model projections of welfare gains due to free trade, coming in the form of increased income and/or increased employment levels, should be treated with some skepticism. This is especially true for the Yukon, since, even in theory, the gains from free trade are not likely to be evenly distributed.

Extrapolating from macro studies in this way to come up with per capital estimates for the average income gain in the Yukon is an exercise fraught with a great deal of difficulty. It is likely to lead to wrong conclusions, and wrong conclusions are likely to lead to bad policy decisions.

<u>The Implications of Free Trade for Canada's Sovereignty</u>

What are the implications of free trade for Canada's sovereignty, broadly defined, and how does this affect the Yukon?

The Prime Minister has said, in the House of Commons and elsewhere, that

> our political sovereignty ... our unique cultural identity ... are not at issue in these negotiations ...

He went on to argue that

> the decision to open negotiations with the United States will not weaken our sovereignty. It is an assertion of sovereignty in an increasingly interdependent world.

It is difficult, however, to see how economic sovereignty, political sovereignty and cultural sovereignty will not be at risk as part of the outcome of the free trade talks.

Moreover, it is difficult to see how this will fail to have a negative effect on the attempts to develop a balanced and diversified Yukon economy in which jobs, citizen participation, environmental protection and cultural safeguards are an important consideration.

Mr. Mulroney is undoubtedly sincere in saying that none of these issues will be subjects for negotiation during the talks themselves. There is reason to think, however, that some of these items are priorities for the American side in the negotiations. Moreover, all of these areas will come under intense pressure in the years after a free trade agreement, as the economy is restructured to meet the new economic conditions.

Let us look at each of these areas inturn.

There are a number of key areas of economic policy in which Canadian practice is likely to come under pressure.

The first of these areas has to do with access to the Canadian market for US investors. This is an area which American negotiators have already said is a priority. Among the areas in which US negotiators will be seeking changes are:

the remaining investment controls in the Investment Canada Act, the successor to the Foreign Investment Review Act

controls on cultural investment, such as investment in book publishing, radio and television stations, magazines

controls on the level of foreign ownership in the chartered banks contained in the Bank Act

controls on foreign investment in the securities and investment business, in such areas as brokerage houses, underwriting and so on

A second critical area in which Canadian policy makers have come under pressure is with respect to the exchange rate. The Secretary of the Treasury has already suggested that the exchange rate of the Canadian dollar is too low, and that this fact will undoubtedly be a subject of some discussion during the trade talks.

As well, a number of business spokespersons have suggested that the Canadian taxation system represents a barrier to full competitiveness, and that in the context of a full free trade pact with the United States it would be important to harmonize the Canadian taxation system with that of the American system so that Canadian businesses can complete,and so that businesses are not driven to relocated in the United States in order to get the benefit of lower American rates.

The dissatisfaction among some American policy makers and politicians with Canadian regional development grants, some aspects of our unemployment insurance system, the stumpage fee system used in Canada to collect royalties on timber, and a wide range of other economic development policies suggests that they will

undoubtedly come under pressure during the talks, and those that survive unmodified will come under pressure in the years after the signing of a free trade deal, either from American interests who feel our policies constitute an unfair subsidy, or from Canadian business interests who object to the relatively high levels of taxation necessary to finance them.

As the MacDonald Commission suggested,

> free trade in transportation or in financial services ... will require the harmonization of diverse national rules governing price competition, service quality, consumer protection and other equally contentious matters ... national tax and subsidy policies concerning petroleum products will need to be harmonized to some extent ...

MacDonald goes on to argue that the tax system will require some harmonization as well.

In the area of cultural sovereignty, America negotiators have suggested that Canadian policies which impeded access to American investment in the entertainment and cultural industries, or which impede access to American products, are a priority for the free trade talks.

Among the policies specifically mentioned are the controls in the Investment Canada Act on foreign investment in cultural industries; lower postal rates for Canadian magazines; the inability of advertisers to deduct as a business expense the cost of advertising on non Canadian radio or television stations; and Canadian content rules in television and radio.

How will these factors affect the Yukon?

In a general sense, the loss of political sovereignty in Canada will affect the ability of the central government to do the sort of economic planning which is required, especially to promote regional development. Moreover, it is equally likely to affect the ability of the Yukon government to plan, and to implement its economic development strategies.

The point is made in the consultant's report submitted earlier, that the effect of free trade would likely be the replacement of political decisions made far away with market related decision that would be more appropriate to the Yukon. The point is made that the population of the Yukon is only one tenth of one percent of the population of Canada, and that this population and one seat in the House of Commons is not enough to guarantee that Yukon interests will always be heard.

However if, instead of political decisions made locally and in Ottawa, the Yukon is made subject to political decisions made in Washington, the situation will be even worse, since the population of Yukon is only one one hundredth of one percent of the population of the United States and the Yukon does not have the benefit of any representation at all in the decision making bodies in the United States.

The Yukon, then would be weakened if the ability of Canadian politicians and policy makers to plan and carry out economic policies is hindered.

The Yukon economy, however, would be even more directly affected if, in the context of a close economic integration with the United States, Canadian monetary authorities were forced to adjust the exchange rate of the Canadian dollar upward - to avoid, for instance, the kinds of disputes over lumber that we have seen recently, or to avoid future disputes over minerals and other raw materials. This is a problem that the Yukon shares with all those areas of the country which depend heavily on the export of raw materials.

As the attached chart demonstrates, the purchasing power parity level of the Canadian dollar has dropped significantly with respect to the US dollar in recent years. It is just that drop that makes many of our goods competitive in the US market, (and just as important, makes many American goods uncompetitive in our market). Moreover, it is the threat that pressure could be brought to bear to adjust the Canadian dollar upward that makes the resource sector of the Yukon and other areas so vulnerable to free trade, since once the Canadian and US economies are more closely integrated, the pressure would be more difficult to avoid or ignore.

With respect to cultural sovereignty, there is obviously a threat to Canadian ownership in the radio, television and magazine industries once any restrictions are removed. There is also the problem of an influx of American programming and American published materials. One could argue that we are already inundated with American cultural and entertainment material; however, the threat is not so much from the American material itself, but from the fact that independent Canadian programming, on radio and television, and Canadian publications, might be squeezed out of the market.

The implications of the squeezing out of Canadian cultural materials is obvious, and threatening; it has economic implications in the sense that Canadian business interests are likely to be harmed. However, it has implications beyond this for the quality of life in the Yukon and elsewhere, since one of the aims of balanced economic development has to be the preservation of traditional cultural values.

Moreover, the domination of Canadian communications by American material, with American values and American political and social

symbols, has political implications in that it would be likely to lessen the social cohesion required to build the political consensus necessary for social and political reforms in Canada.

The Yukon, in brief, is likely to be harmed by any loss of Canadian sovereignty in the general sense that it would affect the ability of governments to do regional development and other economic development work.

The Yukon in particular, might be harmed by the removal of any remaining controls on foreign investment, since it would lessen the possibility of retaining local control over the Yukon economy.

The problems with the exchange rate have been mentioned, but are worth reiterating. Canada would be even more vulnerable under free trade to the kinds of pressures on our exchange rates that could wipe out any economic advantage for many of our goods and services.

Finally, as a society trying to protect some traditional cultural practices and values that are particularly fragile against the onslaught of modern radio, television and other forms of communications the Yukon might be especially harmed by the removal of some cultural programs and policies and by the increased pressure of American entertainment and cultural programming in the Yukon.

Free Trade and Yukon's Development Strategy

The question of how the Yukon should react to the Canada US free trade initiative has to be put in the context of what the economic and social development priorities for the Yukon are likely to be for the foreseeable future.

The most recent, and most succinct, description of Yukon economic and social priorities is given in the Speech from the Throne, three months ago.

The speech listed the priorities as follows:

targeted job creation

economic diversification with local control

open and accountable government

equality of opportunity

improving the quality of life for all Yukon residents

As the Throne Speech suggests

our economic and social futures are firmly linked.

The Speech goes on to note that the Yukon government is working towards a Yukon development strategy,

and that

> this strategy will be based on the Yukon's increased political and economic self reliance. This means promoting the local manufacture of our nature resources as finished products and the increasing use of local labour to provide local services...

The Throne Speech notes that part of the goal of the Yukon Economic Strategy will be to diversity the economy. It notes that while mining, tourism and government will remain central to Yukon economic life, it is necessary to encourage other areas: forestry, manufacturing, food production, energy production and renewable resource development.

As well, the development strategy aims to promote higher levels of self sufficiency, and to identify goods now imported that could be produced locally.

For instance, every year, Yukoners spend $40 million on food, and the effort to provide as large a proportion of the food consumed in the Yukon out of local production is obviously a priority.

All of these are valid, and realizable goals. It is important to ask just how a free trade treaty with the United States would affect the ability to reach these goals.

A look at the distribution of the jobs in the Yukon in 1985 gives some idea of the relative importance of the various sectors.

Forty percent of the jobs in the Yukon in 1985 were in services and trade, while just under 39% were in public administration. Small business and government, then, are the most important sectors of the territory in terms of employment, and a significant proportion of the small business activity is related to the tourist trade.

A little over 5% of the jobs were in construction, about 4% were in transportation, and about 6% were in communications and utilities.

About 7% were in mining and forestry. It is clear that the numbers for 1986, reflecting the reopening of the lead zinc mine at Faro, will have higher proportions for mining, and for the transportation sector as well. It is clear, as well, however, that the mining sector has been the most volatile of the sectors of the Yukon economy, and that it tends to take the rest of the economy with it, in the sense that retail trade, communications and transportation and many other areas of the Yukon economy prosper when mining is prosperous, and suffer when the mining economy is not so prosperous.

(source: Operations and Maintenance Budget Address, 1986-87)
Since virtually all forecasts suggest that commodity prices will be depressed for some time to come, it makes sense to build into an economic development strategy some method of making the economy less vulnerable to the wide swings that characterize the non renewable resource sector in general, and minerals in particular. This would be so even if commodity prices were forecast to be buoyant, but it is particularly important in the next few years.

A comparison of the various forecasts for the 1985-87 period contained in the Yukon Economic Outlook 1985-87 suggest just how much the volatility of the mining sector contributes to the overall volatility of the economy.

In an economy where there are forecast to be about 10,700 jobs in 1986, a little over 1000 of those jobs in 1986 can be attributed directly to the opening of the Curragh mine and the associated spinoff jobs. This is the difference between a forecast of jobs on the assumption that the mine would not open, and a forecast assuming that it would open. While the jobs are obviously welcome, the difference between these two forecasts illustrates just how vulnerable the Yukon economy is without the kind of diversification that, without discouraging mineral production, would make the activity less dominant in the economy, in relation to other activities.

Obviously, diversification of the economy is a long term strategy that will require many years to carry out. Just as obviously, diversification cannot be seen as reducing the importance of the minerals sector, or of discouraging new developments, since they are a valuable part of the Yukon economy; instead, relatively larger amounts of time and effort and funding than is now the case will have to be put into promoting other activities.

It should be noted, as the Yukon Economic Outlook has suggested, that, given the present levels of unemployment, especially in the rural communities, and given the rate at which young people are coming onto the labour market in the Yukon, a rate of growth of about 3% a year is needed just to keep the unemployment rate where it is now, and a rate double that is needed to get it down to reasonable levels within five years or so.

Given the present state of commodities markets, it is not likely that the minerals sector can provide this sort of growth.

Clearly, both economic stability and reasonable rates of growth are critical to developing the kind of society that people desire. Both of these considerations would suggest that diversification is a high priority. That kind of diversification is not likely to come about haphazardly, as a result of uncontrolled forces. It is much more likely to come as a result of economic planning.

Free trade, then, must be put into the context of the kind of economic planning that will go in the Yukon over the next few years. With respect to the kinds of questions suggested in the Throne Speech quoted above, then, the question of how the Yukon should react to free trade depends on an answer to a list of questions something like the following:

> How will it affect the ability of Yukon people to plan their economic future?
>
> How will it affect the ability to diversify the economy into new areas?
>
> How will it affect the ability to develop a stable economy not overly dependent on a small number of economic activities?
>
> How will it affect the ability of Yukon people to keep control of the development in local hands?
>
> How will it affect the number of jobs, and the kind of jobs?
>
> How will if affect equal opportunities, for men and women, for native people, for people in urban and rural communities?
>
> What will be the effect on other "non economic" issues like culture, environmental quality, respect for and preservation of traditional ways of life?

It is not clear that definitive answers yet exist to all of these questions. It is important, however, to ask them.

<u>The Effect On Various Sectors of the Yukon Economy</u>

An examination of the various sectors of the Yukon economy and the possible effect on them of a free trade deal suggest a number of interesting conclusions.

As the consultant's report submitted earlier to the Yukon Economic Council noted,

> many of the benefits and costs of free trade to Yukon are less than obvious and less than certain ... Benefits and costs also depend on many forces outside Yukon's control, such as the value of the Canadian dollar, the strength of the Alaskan economy, and the content of the final agreement.

The consultants in their final report suggest that the sectors that could gain the most from free trade are forestry, mining, transportation and distribution, small scale manufacturing, and that the sectors least affected would probably be government, retail trade, tourism, hunting, trapping, fishing and energy.

About the conclusions of the consultant's report, a couple of comments should be made.

The first is that the report acknowledges, in more than one place, that exchange rates are important economic factors, that changes in the rates could affect the economic calculations around free trade, and that they are largely out of Canada's control.

In fact, the importance of exchange rates as an issue goes beyond the importance given it in the consultant's report. In fact, it has become more likely, since the trade talks have begun and since key American officials have made comments about Canadian exchange rates, that pressure will be put on Canadian rates, in order to move them upward.

Free trade, and the increased inability of Canadian policy makers to resist US pressure, could wipe out the margins that make the minerals sector profitable today, and could endanger the possibility of any new mines opening. Thus the supposed positive effect of free trade on the minerals sector could turn negative very easily.

Moreover, a rise in exchange rates could have a serious negative impact on the tourism industry, which the consultant suggests is not likely to see much impact from free trade.

Further, a rise in the exchange rate would make it impossible for small manufacturers to compete in the Alaska market, a supposed major impact of free trade, and could make it easier for Alaskan manufacturers to compete in the Yukon market.

If the tourism industry is hurt by a rise in the exchange rate, then small business will also be hurt.

Exchange rates, then, turn out to be a lot more important than the consultant's report suggest, and a consideration of the exchange rates problem suggests that free trade is likely to have a major impact, almost all of it negative.

Secondly, the consultant's report appears to have confused the projection of present trends in various sectors with the effect of free trade on those sectors. For instance, in agriculture, a number of possible development areas are suggested; however, it is not clear how they are related to free trade. In fact, as recent EDA reports suggest, there are a lot of things that can be done to stimulate local agriculture as a source of supply for the local market and some of those things are being done now.

Finally, a number of the projections, particularly in retail trade but in others as well, appear to depend on the development of improved transportation and distribution networks.

Clearly, such improvements in transportation and distribution are important, and desirable. the statement is made, however, without any particular proof, that these improvements can be expected to come about as a result of free trade.

In fact, it is possible to come to just the opposite conclusion. Given free trade and some measure of deregulation in transportation, Whitehorse, and even more so the small communities, could wind up being intermediate steps in a transportation network based on Alaska. Given the larger population and larger business community in Alaska, and given both the small population in Yukon and the great distances between population centres, the result of free trade combined with some measure of deregulation could well be a deterioration in the quality of transportation services, and a centralization of distribution networks around Anchorage rather than Whitehorse.

In short, neither Whitehorse nor the smaller communities have any particular reason to think that free trade, by itself, will result in improved transportation and distribution networks. If that is the case, then the positive impact suggested in the consultant's report, which is based on such improvements, is difficult to foresee.

Clearly, transportation is critical to the Yukon. If it appears that free trade would mean a deterioration in transportation and distribution facilities, then free trade should be opposed on that ground alone.

However, it should be clear that if development depends on such improved transportation and distribution networks, as it does, then the various levels of government should concentrate on this area specifically, rather than assuming it will come as a result of other economic initiatives like free trade. Waiting for free trade to make things better in this area might mean, in fact, that the hoped for improvements will never come.

A brief discussion of the various sectors, and the consultant's treatment of them, follows.

Agriculture

The consultant's report suggests that the impact of free trade on the agricultural sector is likely to be small, but that it would probably be positive.

As noted above, however, the assumption of a positive impact seems predicated on improvements in transportation, which are not necessarily related to free trade.

The consultant's report notes that there is some chance that the local demand for potatoes and some other vegetables, for dairy, eggs and other poultry, and for hay, could be filled, locally rather than with imports. The possibility of a farmers' market in Whitehorse is also mentioned. All of these are desirable; however, it is not clear why the possibility of any of them is tied to free trade. Recent EDA initiatives, for instance, have involved support for a greenhouse that could supply a significant proportion of the local market for tomatoes, support for egg production, support for the development of an elk herd. EDA has also commissioned a study on import substitution in the agricultural area. All of these things are useful initiatives, and none of them are tied to free trade.

Forestry

As the consultant's report suggests, the impact of free trade on the forest sector is likely to be small, and many years in the future. However, the end of local procurement policies could have an impact on the purchase by government in the Yukon of locally produced wood articles.

As recent events suggest, access for lumber to US markets is not likely to be materially improved by free trade, since the ability to apply countervail to various types of wood products will remain even after a free trade deal is signed. In fact, more likely is the fact that access for lumber to the US market would be traded off for access to other products, such as manufactured goods. As well, of course, access to the US market depends on favourable exchange rates continuing, which is less and likely given American pressure on our exchange rates.

Hunting and Trapping

Again, the impact of free trade on this sector is likely to be minor. The possibility of lower cost supplies depends as much on improvements in transportation as on free trade, and, as noted, there is no particular reason to link the two.

Commercial and Subsistence Fishing

There are currently no tariffs on fish exports to the US, so the only foreseeable positive impact of free trade on this area would be the chance of getting lower cost supplies; again, this depends on improved transportation networks. As the consultant's report suggests, the most important constraint on fishing in the Yukon is resource access, not market access.

Mining

Clearly, the jobs potential of mining makes it an important element of economic planning, even if attempts are made to diversify. The consultant's report suggests that mining could see major benefits from free trade, and this would suggest supporting free trade for its impact on the Yukon economy if the positive impact were one that we could confidently predict.

However, there is no particular reason to think that lower cost inputs would be a major result of free trade with the US, since, again, this depends to a great extent on transportation improvements that are less than certain.

The most important factor to be taken into account here would appear to be the effect of rising exchange rates. To the extent that free trade makes it more difficult to resist American pressure to raise exchange rates then free trade could have a negative impact on the mining industry, especially since it would appear that the combination of low commodity prices and alternative sources of supply make this an industry very vulnerable to economic change.

As well, as the comments made earlier suggest, free trade with the US, if it is interpreted as part of a move to erect trade walls around North America, could invoke retaliation from trading partners in the Orient. Since supply side competition for most minerals is the case, this retaliation could take the form of switching to an alternative source of supply.

All in all, there is no particular reason to think that free trade would be good for the Yukon minerals sector, and it could turn out to be very negative.

Oil, Gas and Other Energy

In this area, again, the impact of free trade is likely to be small. International energy prices will be the determining factor for the rate of development in this industry.

Tourism

There are virtually no trade barriers that directly affect the Yukon tourism sector now, so the direct impact of free trade is likely to be small. However, changes in the exchange rate could have a devastating impact on the tourism industry, and if free trade makes us more vulnerable in this area, then it should be opposed.

Again, much of the suggested impact on free trade depends on improved transportation systems. This is obviously something that is highly desirable, for its impact on the tourist trade, but it is not clear how it is connected to free trade.

Manufacturing

It is suggested that simplified customs procedures could make it simpler for small manufacturers to ship into the Alaska market. This hope may be overblown, however. It will still be necessary to go through some procedure of recording shipments, prices and so on, if only so that US trade officials can keep track of imports and their impact on US jobs and industry. The notion that goods will simply flow across the border as if it did not exist seems without merit. Certainly, in the case of the autos, this is not the case. And it is certainly not the case with softwood lumber, for which there are no tariffs at present. While customs procedures may be simplified to some degree, they will not be eliminated.

The problem of rising exchange rates has already been mentioned. This is clearly a factor here, and potentially a very negative one. This is even more the case with manufacturing than with some other areas, since a rise in the exchange rate would not only make Alaska goods more competitive here, possibly leading to damage to Yukon businesses in the specialty manufacturing area.

Construction

The impact of free trade here is likely to be small, since this is an industry that is very locally oriented. While some Yukon companies could possibly compete in the Alaskan market, the possibility of Alaskan companies competing in the Yukon has also to be taken into account.

Transportation, Wholesale, Distribution

The point has already been made that this is not necessarily connected with free trade.

In fact, historically, improvements in transportation have depended heavily on government support. To the extent that government support is limited because of free trade, then transportation could be damaged.

Business and Professional Services

Again, the possibility of competing in the Alaska market has to be balanced off against the likelihood that Alaskans will compete in the Yukon as well. If the restrictions on such things as cross border advertising are a victim of the free trade talks, as is possible, then the result could be damage to Yukon radio stations and to Yukon based advertisers. Certainly access for a wide range of services is high on the American list for the free trade talks. This could include engineering services, financial services, computers and data processing, clerical services, and so on. The result could be intense competition in the service sector, from which Yukoners in this sector could suffer.

Retail Trade

As the consultant's report notes, the strong local market orientation means that retail trade would not be affected very much in a direct way from free trade; the possibility of competing in the Alaskan market has to be balanced off against the increased competition from Alaskan businessmen; most of the benefits again seem to be from improved transportation and distribution systems, not from free trade; there is the chance of lower prices from consumers, but there is no particular guarantee that, in an environment where there is little competition, the benefits will not accrue in the form of higher profit margins, not necessarily in the Yukon, rather than lower prices.

Government

The impact on government is likely to be small, confined to some lower cost inputs, which depend as much on improved transportation networks as on free trade; there is the possibility that some regional development and other programs of the federal government could be affected by free trade; there is also the chance that the ability to use government procurement as an economic tool could be limited as well.

In sum, it is difficult to find a dramatic change that is likely to happen in the Yukon as a result of Canada/US free trade. The most significant change, in the mining sector, is highly speculative in light of weak commodity prices and alternative sources of supply, and in light of the vulnerability of the industry to changes in exchange rates. The effect here is likely to be negative.

The same is true in the tourism sector.

In the other sectors of the economy, those areas where diversification could create jobs and produce a more stable economy, there is no particular reason to think that free trade will encourage this process.

In fact, the most important element in diversifying the Yukon economy into new areas is likely to be the ability of the Yukon and federal governments to plan and carry out programs that will have this effect. If the outcome of the free trade talks, or the aftermath, is a significant weakening of Canadian sovereignty, then the ability of both levels of government to carry out these programs may be weakened.

An Analysis of the Consultant's Recommendations

1. The agreement should be broad in scope, include both tariff and non tariff barriers and trade in both goods and services. Presumably it will, since it needs to be in order to qualify under GATT, Article XXIV.

2. The agreement should be open to participation from other countries. Again, in principle, it needs to do this to quality under GATT.

3. It should not jeopardize our existing international trading relationships and responsibilities. This is more difficult. The motivation in the US from special trading relationships with other countries, such as Israel and now Canada, is precisely to demonstrate to other countries that the US means business. Presumably, then, if the motivation is to reduce the US trade deficit, we will not be able to use Canada as a trans shipment point for cheap goods whose destination is the US. The DPA report suggests that "Canada US free trade should be viewed as a forward step in liberalizing international trade, not as the establishment of 'fortress North America'". This, of course, is easier said than done, especially since this seems to be a major motivation for the free trade deal as far as the US is concerned.

4. The dispute settling mechanism should be non political. This is impossible, and the only precedent, the IJC, does not work very well. It is unlikely that the US would give up its sovereignty in this regard to an international body. All decisions would always be subject to Congressional ratification, and US law supersedes international agreements.

5. The transition period has be to long, minimum 5 years, and should be at least 5 years longer than the US transition period. The likelihood of getting this on tariffs is very low, and on non tariff barriers just as unlikely.

6. The deal should not compromise Canada's social programs, cultural programs, regional development programs. We an assume that none of this will be in the final document, although all of these things have been mentioned, and the cultural, especially, is on the US list as high priority items. But we can assume that in the climate after the free trade deal all of these things will come under a great deal of pressure.

7. Foreign investment policies should allow the YTG to protect vulnerable industries from overinvestment and too rapid development. The Americans are already unhappy with us. We can assume that the repeal of the Foreign Investment Review Act was done under US pressure, and still the Americans are unhappy with what is left of investment controls under the Investment Canada Act. Control over investment is liable to be traded away in a free trade deal.

8. Federal government should provide support for improvements in transportation and communications systems. This should happen anyway, and in no way should be seen as tied to a free trade deal. This suggestion, in fact, illustrates the danger of tying a number of developments to a free trade deal with the US when they are the kinds of things that we should be working on anyway, with or without a free trade deal.

Another point is worth making here about the conclusions reached in the consultant's report, although it is mentioned elsewhere as well.

There is some reason to think that regional development programmes are under threat in the free trade talks as non tariff barriers, and that the ability of governments to engage in this activity might be threatened. The consultant's report suggests that this is not likely to affect the programs carried on by the Yukon government since they are small scale and do not involve the expenditure of large amounts of money.

There are two problems with this argument. The first has to do with the fact that it is a major priority of the current government, and presumably will be a priority of future governments, to get both increased funding and increased powers to carry on development activities. In future, the Yukon government might find itself carrying on economic development programs of the type that are now done by the federal government, and with the aid of revenues larger than is the case today. If that were the case, the argument that no one in the United States is likely to notice our programmes would no longer hold.

However, even with our present programs, it should be noted that under US law, trade related actions are not usually initiated by government, but by local industries or businesses that are affected. In short, it is not likely to be the government, but business concerns in Alaska that will raise concerns about our policies. This has been the case with cedar shakes and shingles, with softwood lumber, with east coast fish, and with a number of provincial and federal programs that are seen as constituting unfair subsidies, as with the case of east coast fish.

Risks to the Yukon From Free Trade

In sum, then, the negotiation of a free trade deal with the United States could have a significant impact on the Yukon economy.

Among the dangers are the problems of the vulnerability of several sectors to changes in the exchange rate, and the fact that Canada would be more subject to pressure in this area after a free trade pact.

The mining industry and the tourist industry seem particularly vulnerable in this respect, but other sectors, such as small manufacturing, could have problems as well.

There is also the problem of increased competition from Alaska, which could threaten Yukon small business and some service industries.

More generally, if free trade results in the deterioration of some social programs, or in regional development or other programs, then the quality of life for most Canadians, including those in the Yukon, could suffer.

Cultural sovereignty is an important element in defining the life of a country, and preserving cultural traditions is important. This is particularly important in the north, where native cultural traditions have already been under pressure from radio, television and other forms of mass communications. Free trade would undoubtedly make this problem worse.

The problems of controlling foreign investment have already been mentioned, and this must be taken into account as well, if maintaining local control is an important element in an overall strategy designed both to protect the natural environment, to create local jobs, and to maximize the quality of life for most people in the Yukon.

Overall, however, the most serious negative impact of free trade, both in the Yukon and elsewhere, may lie in the tendency to assume that free trade alone will accomplish the economic restructuring that is necessary for the Canadian economy. In order to develop the Yukon, economic planning and careful coordination will be necessary. This will mean different levels of government and the private sector working together on the assumption that economic development cannot be left to haphazard events. If, after three or four years, the free trade initiative falls apart, as increasingly it looks as if it might, then the worst aspect of free trade will be that it will have represented a detour of several crucial years in which economic planning and the consensus building necessary to carry out economic plans could have been developed. Ultimately, this may be the most important, and the most tragic, legacy of the free trade debate.

How Should the Yukon Government React?

The questions arises, then, of what the reaction of the Yukon government should be to the free trade initiative.

As this brief has suggested, there are enough possible negative aspects to free trade that the Yukon should be extremely reluctant to endorse free trade as a way to restructure the Yukon economy.

The MacDonald Royal Commission on the Economy, which endorsed the idea of free trade, referred to it as a "leap of faith". Clearly, governments which have responsibility for the economic and social welfare of their citizens have to operate on something a bit more substantial than faith. The brief has suggested enough substantial concerns about the impact of free trade that the government should not consider simply endorsing the idea of free trade.

The consultant's report suggests that the Yukon government endorse free trade because of the perceived political advantages of siding with a government which is likely to be grateful for any support which it receives. Aside from the fact that this approach is not likely to produce the benefits suggested, it is a particularly inappropriate response to an economic change which could potentially have a dramatic effect on the lives of all Canadians, including those in the Yukon.

To the extent that approval for free trade puts other things on hold, the Yukon suffers. A better strategy would be to say to the federal government that the Yukon expects development projects to go ahead, not be delayed by the possibility of a free trade arrangement.

Since free trade is part of a back to the market philosophy, it should be made clear to the federal government that free trade talks must not be allowed to compromise the ability of the federal and territorial governments to influence the pace and kind of economic and social development that takes place in the Yukon.

It remains the fact that a lot more research needs to be done on the impact of free trade on various industries, and on various regions. However, the information which we now have suggests that the effects of free trade, both in the short term and in the longer term, might be negative for Canadians. This is true on both economic grounds, and on wider grounds as well.

We are currently on the verge of another round of multilateral trade talks under the GATT. In the past these talks have proven remarkably effective in reducing trade barriers and liberalizing world trade, to the benefit of all or most of the participants. There is every reason to think that the result of the next round will be similarly beneficial to the world economy, and that Canada should firmly endorse the idea that trade issues should be settled in a multilateral forum.

If as suggested in this brief, bilateral and multilateral solutions to Canada's trade problems are mutually exclusive, in that the bilateral route will lead to our becoming associated with a form of American protectionism that is not good in the long run for either Canada or the world economy, then we must choose one or the other.

It would the firm recommendation of the labour movement that the Yukon place itself on the side of the multilateral solutions to the trade problems which face us, and that we reject the option of bilateral free trade talks with the US. A free trade arrangement would not be good for Canada, and especially would not be good for Yukoners.

APPENDIX I

Trade Related Measures Under the GATT

GATT measures which allow a member country to interfere with the imports of another nation include the following:

Article VI allows countervailing duties or additional duties above a country's regular tariff rate to off set undervaluation due to such a subsidy if the subsidy causes or threatens material injury to domestic industry. This article also permits an importing country to impose anti dumping duties, over and above any normal customs duty, to overcome the injury done to a domestic industry when the product is sold on the export market a price lower than the normal or internal value of that product in the exporting country's home market. The provisions of Article VI are dealt with in the Special Import Measures Act, proclaimed in 1984, which replaces the Anti Dumping Act,and which established the Canadian Import Tribunal, the Canadian equivalent to the US International Trade Commission. The current attempts to impose countervailing duties on Canadian softwood lumber exports to the United States are specifically allowed under this provision of GATT.

Article XI allows the use of quotas to control imports if it is operated in conjunction with a government domestic supply control program. Under Article XI, the Canadian Export and Import Permits Act allows for the establishment of export or import quotas on agricultural commodities (and other items) to ensure an adequate supply of the commodity in Canada, and to support and implement various agricultural policies.

Article XVI allows subsidies to assist exports of agricultural or other primary products as long as the subsidies do not result in the subsidizing country obtaining "more than equitable share of world export trade in that product".

Article XIX allows for emergency procedures to prevent serious injury to domestic producers from an increase in quantities of imports of similar or directly competitive products. It is under this provision, and the American legislation which is consistent with it, that the US tariff on cedar shakes and shingles was imposed.

Articles XX and XXI permit restrictions on imports for health, safety, security and other special reasons. Under this Article, there are a large number of Acts, such as the Meat Import Act, the Meat Inspection Act, The Food and Drug Act and the Consumer Packaging and Labelling Act. US attempts to curtail Canadian exports of hogs and dressed pork are consistent with this provision of GATT.

APPENDIX I (continued)

All of these measures are allowed under Gatt practice, and the GATT articles have their counterparts in Canadian legislation, and legislation in other GATT countries, which gives effect to these provisions.

APPENDIX II

Non Tariff Barriers

In addition to the GATT measures listed above, Canada has been able to enact a whole series of what are, in effect, non tariff barriers designed to meet certain national policy goals. Some of these include:

Global quotas, prohibitions and other import controls, which affect products such as footware, butter, milk and milk powder, wheat, oats, barley, eggs, poultry, used cars, used aircraft, and the import monitoring and surveillance of a large range of other products.

Voluntary export restraints on automobiles from Japan, textile products and clothing products from many Third World countries under the Multi Fibre Arrangement.

Government procurement policies in effect in all federal and provincial governments and Crown Corporations which favour Canadian suppliers, often with provisions giving preference to Canadian suppliers even if they are not the most favourably priced bidder.

Provincial and Territorial Liquor Commission monopolies which provide, in Ontario, the Yukon and elsewhere, for markups in price for imported goods and for listing policies which favour domestic products.

A customs procedure system which in many cases requires "made in Canada" or"country of origin" stickers and labels.

Performance requirements and domestic content requirements such as those which formerly existed under the Foreign Investment Review Act and some of which continue to exist under the Investment Canada Act; similar ownership restrictions which limit the extent of foreign ownership of Schedule A banks (full service Canadian owned banks) and which limit the asset size of Schedule B banks (foreign owned banks): differential subsidy programs based on ownership under the National Energy Program.

Cultural protections such as the disallowance as a business expense of advertising costs on non Canadian broadcasting stations and in non Canadian magazines; Canadian content requirements on Canadian radio and television stations; differential postal rates to Canadian magazines and periodicals; the special provisions in the Investment Canada Act relating to foreign investment in sectors deemed vital to our cultural identity.

APPENDIX II (continued)

Subsidies such as those under the Shipbuilding Industry Assistance Program, which provides subsidies for purchases of Canadian built ships; capital subsidies such as those under the Defence Industry Productivity Program, General Development Agreements, Industrial and Regional Development Program, Canadian Industrial Renewable Board, provincial subsidies for purchase of fishing equipment; a whole series of research and development subsidies such as the recently discontinued Scientific Research Tax Credit, the Industrial Research Assistance Program, Energy Research and Development Program, Enterprise Development Program, New Technology Employment Program, others.

Transportation subsidies such as the Crow's Nest Pass Agreement and its successors, Maritime Freight Rates Act, Atlantic Region Freight Assistance Act, transportation subsidies for feed grain.

Sport subsidies for skim milk powder; subsidies under the Program for Export Market Development, Promotional Projects Program, subsidized export financing provided by the Export Development Corporation.

Duty remission programs designed to stimulate domestic investment in autos and parts, power cruisers, televisions and parts, sewing machines, off highway vehicles.

Bilateral tied aid programs that provide conditional aid in the form of feed grains, powdered skim milk, electrical machinery and equipment, rail transportation equipment.

Product standards such as those for some electrical products.

The service account balance is expected to improve in 1986, and to deteriorate in 1987 and 1988 but at a much slower rate than in recent years (chart 17). The major positive factors this year will be a likely $1 billion cut in the travel deficit due to Expo 86, a reluctance on the part of North American tourists to travel to Europe, and the relative attractiveness of the Canadian dollar. Over the entire forecast period the predicted lower interest rates and appreciating currency will bring down the growth in net interest payments abroad, although net foreign indebtedness in itself is still expected to grow by a sizeable amount.

The Capital Account and the Canadian Dollar

Over the forecast period, we do not expect the capital account to provide much support for the Canadian dollar. Net direct investment flows are likely to remain negative, though nowhere near as large as 1985's $7.4 billion. Canadian business has become more active in the U.S. and a few other countries over the last decade, and since this new Canadian multinationalism is forecast to continue, a steady outflow of capital can be expected. At the same time, the process of repatriation of foreign investment in Canada, which received such a push from the National Energy Program, does not appear to be coming to an early end, while the flow of new investment by foreigners has provided no major offset, in spite of Ottawa opening the door wider to foreign investment.

As discussed on page 16, Canada is expected to reduce its reliance on foreign markets for new borrowings in coming years. Nevertheless, 1986 is shaping up to be a near-record year, with net foreign purchases of Canadian securities over $9 billion. A large share of this financing has already taken place in the first four months of the year, as interest rate spreads opened up as a result of Bank of Canada open market activity in support of the dollar. However, just as we forecast that the current account will move towards balance in 1988 so do we look for Canada to move closer to being a net exporter of capital by 1988 and interest rate spreads between Canada and the U.S. to be virtually eliminated.

The weakness of the Canadian dollar vis-a-vis the U.S. dollar since last November was, in our view, largely the result of foreigners' perceptions of mismanagement of monetary and fiscal policy as well as reflecting the perceived effects on the Canadian economy of weak commodity markets. We think that most foreign exchange participants now view Canada more favourably. Thus, the Bank of Canada has already been able to lower interest rate spreads at the short end to about 180 basis points by mid-May from a high of over 430 in early March. Long rate spreads, which have risen by more than 130 basis points since November, are also forecast to narrow soon. We expect the Canadian dollar to continue to move closer towards its purchasing power parity level (chart 18) over the next two to three years allowing interest rate spreads to narrow further.

CHART 17

DETAIL OF CURRENT ACCOUNT AS A PERCENT OF GNP

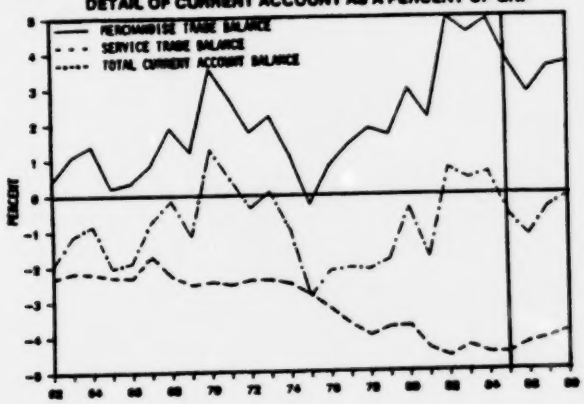
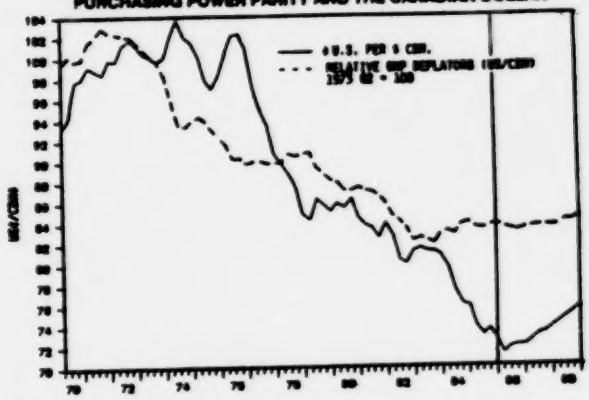


CHART 18

PURCHASING POWER PARITY AND THE CANADIAN DOLLAR



A = Actual
F = Forecast
P = Preliminary

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Source for Historical Data: Statistics Canada, Bank of Canada, OECD, U.S. Dept. of Commerce, U.S. Dept. of Labour and U.S. Federal Reserve Board. Certain data originated from CANSIM which is the registered Trade-Mark of Statistics Canada's machine-readable data base.

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